

Internal Revenue Service

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December 18, 2015

LEGEND

Trust =

A =

B =

X =

State =

To Whom It May Concern:

This is in reply to your letter of June 8, 2015, and supplemental correspondence, submitted on behalf of Trust requesting a ruling under section 1361(d)(3) of the Internal Revenue Code ("Code") that Trust is eligible to be a Qualified Subchapter S Trust, and thus an eligible shareholder of X, an S corporation.

FACTS

A created Trust for the benefit of child B. B is a citizen of the United States.

Article Seventh, Section 3 of the trust agreement provides that the income from Trust shall be paid in convenient installments, at least quarterly, to B until complete distribution of the trust or his prior death.

Article Seventh, Section 3 of the trust agreement further provides that “[t]he trustee may also pay to the child such sums from the principal of Trust as the trustee deems necessary or advisable from time to time for the health, maintenance in reasonable comfort, education (including postgraduate) and best interests of the child and his descendants, individually and as a group, considering the income of each of them from all sources known to the trustee. No payment made for a descendant of the child shall be charged against the share hereinafter provided for the descendant or his ancestor or descendants.”

Article Seventh, Section 3 of the trust agreement continues to provide “[i]t is my intention that my child be the primary beneficiary of Trust. Accordingly, the trustee may disregard the interests of the remaindermen of such Trust in the investment of the trust assets and in making discretionary distributions of trust property to the child.”

Pursuant to the laws of State, which govern Trust, interested parties may enter into a binding, non-judicial settlement agreement with respect to the validity, interpretation, or construction of the terms of a trust that is final and binding on the trustee, on all beneficiaries of the trust, both current and future, and on all other interested persons as if ordered by a court. Pursuant to this procedure, the trustees and beneficiary of Trust entered into a non-judicial settlement agreement regarding the administration of Trust. Under the terms of the agreement each party agreed:

1. That the power of the trustees to distribute the principal of Trust pursuant to Article Seventh, Section 3 of the trust agreement is limited to a distribution to B, and is not for the benefit of any other person during the life of B.
2. That the terms of the trust agreement governing Trust do not authorize or permit distributions of principal to any descendant of B, directly or indirectly, during the life of B, and that principal distributions from Trust may only be made for B's benefit.
3. That the provisions of Trust do not create, nor did A intend to create, any right, claim or cause of action in any such descendant, as against B or the trustees, to compel or require B or the trustees to pay over any part or all of a principal distribution to such descendants, or any of them, whether or not the trustees took into account the health, maintenance in reasonable comfort, education and best interests of

those descendants in determining the amount of the principal distribution.

LAW

Section 1361(d)(1)(A) of the Code provides that in the case of a qualified subchapter S trust, with respect to which a beneficiary makes an election under section 1361(d)(2), such trust shall be treated as a trust described in section 1361(c)(2)(A)(i) (relating to trusts that may be shareholders of a “small business corporation” under section 1361(b)(1)).

Section 1361(d)(1)(B) provides that, for purposes of section 678(a), the beneficiary of a qualified subchapter S trust shall be treated as the owner of that portion of the trust consisting of stock in an S corporation with respect to which the election under 1362(d)(2) is made.

Section 1361(d)(2) provides, in general, for the time and manner in which a beneficiary of a qualified subchapter S trust may elect to have the provisions of section 1361(d) apply.

Section 1361(d)(3) defines the term “qualified subchapter S trust” as a trust all of the income (within the meaning of section 643(b)) of which is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States. In addition, the terms of the trust must require that during the life of the current income beneficiary there shall be only one income beneficiary of the trust; any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary; the income interest of the current income beneficiary in the trust shall terminate on the earlier of such beneficiary's death or the termination of the trust; and upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to such beneficiary.

Section 643(b) provides that for purposes of subpart A, B, C, and D of the Code, the term “income”, when not preceded by the words “taxable”, “distributable net”, “undistributed net”, or “gross”, means the amount of income of the estate or trust for the taxable year determined under the terms of the governing instrument and applicable local law. Items of gross income constituting extraordinary dividends or taxable stock dividends which the fiduciary, acting in good faith, determines to be allocable to corpus under the terms of the governing instrument and applicable local law shall not be considered income.

Section 1.643(c)-1(a) of the Income Tax Regulations provides that the term ‘beneficiary’ includes any person with respect to an amount used to discharge or satisfy that person's legal obligation as that term is defined in section 1.662(a)-4.

Section 1.662(a)-4 provides, in part, that any amount which, pursuant to the terms of a will or trust instrument, is used in full or partial discharge or satisfaction of a legal obligation of any person is included in the gross income of such person under section 662(a)(1) or (2), whichever is applicable, as though directly distributed to him as a beneficiary.

CONCLUSION

Based on our examination of the trust described above, and the additional information submitted, we conclude that Trust meets the requirements of section 1361(d)(3) of the Code. Except as specifically ruled upon above, no opinion is expressed concerning the federal income tax consequences of the transaction described above under any other provisions of the Code. Specifically, no opinion is expressed concerning whether X meets the requirements of a small business corporation under section 1361(b) of the Code.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the power of attorney on file with this office, we are sending a copy of this letter to your authorized representatives.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the ruling request, it is subject to verification on examination.

Sincerely,

Bradford R. Poston
Senior Counsel, Branch 3
Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)
Copy of this letter
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